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No. 90-1290

Supreme Court, U.S.
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In The Supreme Court of the United States October Term, 1990

EDWARD F. BAGDON,

Petitioner,

v.

THE FIRESTONE TIRE AND RUBBER COMPANY,

Respondent.

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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Respondent's attempt to support the decision and judgment of the Seventh Circuit fails as much because of what it does not say as because of its misstatements.

I. RESPONDENT CANNOT DISGUISE THE CONFLICT BETWEEN THE SEVENTH CIRCUIT'S DECISION AND THIS COURT'S PRIOR DECISIONS.

Of utmost importance, Respondent has not cited and cannot cite any other case holding, as the Seventh Circuit held here, that "Rule 19 is *not* "applied pragmatically" in derivative cases." The reason why no such case exists (until now) is because this Court explicitly held in *Provident Tradesmens Bank & Trust Co. v. Patterson,* 390 U.S. 102 (1968) that Fed.R.Civ.P. 19 must

be applied pragmatically in all cases, even derivative actions. 390 U.S. at 119. The Seventh Circuit's attempt to create an arbitrary exception to this rule for derivative cases directly contravenes this Court's mandate and is reason enough for granting the petition.

Rather than recognizing that *Provident Tradesmens Bank* is controlling here, Respondent attempts to assert that it does not apply while also contending that the Seventh Circuit somehow complied with its dictates. However, Respondent cannot have it both ways. In the first place, the only question here is whether the parties' corporation is a necessary party under Fed.R.Civ.P. 19 — a question governed by *Provident Tradesmens Bank,* not by the cases cited by Respondent (or the Seventh Circuit) which did not even involve the present version of Rule 19.[1] Second, Respondent's assertion that the Seventh Circuit's decision can be reconciled with *Provident Tradesmen Bank* is ludicrous since the Seventh Circuit never even mentioned that case and *expressly refused* to apply the pragmatic approach mandated therein.

II. RESPONDENT DOES NOT DENY THAT THE SEVENTH CIRCUIT CREATED A SPLIT AMONG THE CIRCUITS.

Respondent also does not dispute that the Seventh Circuit created a split among the Circuits by refusing to accord any deference to the District Court's Fed.R.Civ.P. 19 determiniation that Petitioner's claims were *not* derivative and that the parties' corporation was not a necessary party. Instead, Respondent affirmatively misstates the record in asserting that Petitioner "did not brief the standard of review to the Seventh Circuit",[2]

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[1] Significantly, all of Respondent's cases, including *Ross v. Bernhard,* 396 U.S. 531 (1970) (initially filed in 1965), arose *before* the important 1966 amendments to Rule 19 and this Court's decision in *Provident Tradesmens Bank* which mandated a pragmatic application of Rule 19 with a focus on the realistic analysis of the facts of each case. In *Ross,* the parties never even disputed whether their corporation was a necessary party — only whether plaintiffs were entitled to a jury trial on their derivative claims.

[2] Petitioner extensively briefed this issue to the Seventh Circuit in his motion for rehearing.

as if that somehow excuses the conflict among the Circuits created by the Seventh Circuit's *de novo* review here. As Respondent does not and cannot deny, every other Circuit which has considered the issue has adopted an "abuse of discretion" standard of review.

Respondent's blind insistence on justifying the mechanical rule adopted by the Seventh Circuit here is perhaps the best evidence that the practical and pragmatic application of Fed.R.Civ.P. 19 in *this* controversy could only have resulted only in a finding that the parties' corporation was *not* a necessary party. Indeed, Respondent cannot point to any interest of the parties' close corporation which is separate and apart from those of its two shareholders.[3] As the District Court properly found and Respondent does not deny, complete relief could be granted in the absence of the close corporation, no third party could be prejudiced by any judgment rendered on behalf of petitioner and against respondent, and no threat of multiple litigation existed since all necessary parties were already before the court.

Now, for the first time, Respondent asserts that the Seventh Circuit's finding that Petitioner's claims were derivative somehow eliminated the need for any further analysis as to whether the parties' corporation was a necessary party. Respondent is simply wrong. Petitioner's claims were individual in nature because Respondent breached fiduciary duties which it owed *directly* to Petitioner and inflicted *individual* injuries upon Petitioner not shared by Respondent or the close corporation. But more importantly, even the Seventh Circuit recognized that Petitioner's claims "involve[d] some injury external to the store-corporation" (916 F.2d at 381). Hence, under the undisputed rule in Delaware (and elsewhere), Petitioner should have been allowed to proceed individually since his claims involved both individual and derivative injuries, even assuming the primary injury was to the corporation. *Elster v. American Airlines, Inc.*, 24 Del. Ch. 94, 98-99, 100 A.2d 219, 212 (1953); R. Balotti and J. Finkelstein, *The Delaware Law of Corporations and Business Organizations*, Sec. 13.6, p. 626 (1989 Suppl.).

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[3] Indeed, the close corporation has no practical existence apart from the two shareholders since Respondent abolished the close corporation's Board of Directors after changing the state of incorporation from Illinois to Delaware.

Finally, even assuming, *arguendo,* that Petitioner's claims were completely derivative in nature (which the Seventh Circuit did *not* hold), the Seventh Circuit completely misstated Delaware law as requiring the joinder of the parties' corporation in all cases involving derivative claims. The very case relied upon by Respondent and the Seventh Circuit, *Taormini v. Taormini Corp,* 32 Del. Ch. 18, 78 A.2d 473 (1951), explicitly recognized that a minority shareholder *can* bring derivative claims individually where, *inter alia,* manifest injustice would result or the corporation's rights would not be protected otherwise.[4] *Id.* at 475. This is consistent with the modern rule recognizing that where, as here, the reasons for requiring a shareholder to proceed derivatively are not present, the parties' corporation is *not* always a necessary party.

Thus, under any analysis other than the one rejected by this Court in *Provident Tradesmen Bank,* but adopted by the Seventh Circuit here, this litigation, which has already been tried to conclusion, should have been allowed to proceed without the unnecessary and meaningless joinder of the parties' corporation and then another full trial in state court.

III. RESPONDENT DOES NOT DISPUTE THAT THE SEVENTH CIRCUIT ABUSED ITS APPELLATE JURISDICTION.

Respondent also concedes by silence that the Seventh Circuit made an erroneous and improper factual finding that the parties' corporation was incorporated in Delaware for choice of law purposes, even though it was in fact an Illinois corporation during the operative events giving rise to liability. Instead, Respondent merely argues that this fundamental error somehow did not make a difference. However, the Seventh Circuit's abuse of its appellate jurisdiction caused it to apply Delaware law which in turn led to an erroneous finding that Petitioner's claims were derivative in nature and, therefore, required the joinder of the parties' corporation. However, not only was the Seventh Circuit's view of Delaware law patently erroneous, Petitioner's claims were undoubtedly individual in nature under Illinois law. *Graham v.*

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[4] The Seventh Circuit's failure to follow Delaware law clearly has constitutional implications under the *Erie* doctrine.

Mimms, 111 Ill. App. 3d 751 (1st Dist. 1982); *Zykoych v. Spalding*, 36 Ill. App. 3d 654 (1st Dist. 1976). Moreover, the Seventh Circuit's erroneous application of Delaware law is also clearly contrary to the result which would have occurred under Ohio law, had the Seventh Circuit deferred to the District Court's choice of law determination. *Crosby v. Beam*, 47 Ohio St. 3d 105, 548 N.E.2d 217 (1989).

CONCLUSION

The controversy before this Court is not the petty squabble over the proper interpretation of Delaware law, as Respondent understandably attempts to paint it. Rather, it concerns a Seventh Circuit decision that directly conflicts with, indeed flaunts, this Court's precedent, creates a conflict among the Circuits and involves a fundamental abuse of its appellate jurisdicition. The result is unjust and elevates form over substance to waste judicial resources by forcing a retrial in state court. For all of the above reasons and the reasons set forth in his initial brief, Petitioner, Edward F. Bagdon, respectfully requests that this Court grant his petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit and enter an Order reversing the Seventh Circuit's dismissal of his cause for failure to join a necessary party.

Respectfully submitted,

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